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IN THE

Supreme Court of the United States

State Farm Mutual Auto Ins. Co.,
Petitioner,

v.

Curtis B. Campbell, *et al.*,
Respondents.

On Writ of Certiorari
to the Supreme Court of Utah

BRIEF *AMICUS CURIAE* OF UNITED POLICYHOLDERS

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BRIEF *AMICUS CURIAE*

United Policyholders respectfully submits this brief as *amicus curiae* in support of respondents.[1]

INTEREST OF THE *AMICUS*

Amicus United Policyholders ("U.P.") is a non-profit organization founded in 1991 to educate the public on insurance issues and consumer rights. The organization is funded by donations and grants from individuals, businesses, and foundations.

U.P. fulfills its mission in several ways. First, it serves as a resource for insureds by providing consumer-oriented insurance information through publications and programs. Second, U.P. monitors developments in the insurance industry that may affect the interests of all insureds. Because of its familiarity with these developments, U.P. receives frequent invitations to testify at legislative and other public hearings and to participate in regulatory oversight proceedings. Third, U.P. communicates with a diverse range of insureds throughout the United States regarding the insurance claims process. Based on its monitoring of legal and marketplace developments and the real-life experiences of insureds, U.P. regularly submits *amicus curiae* briefs to provide appellate courts around the country with the policyholder's perspective in cases involving insurance principles that are likely to have a widespread impact. See, *e.g.*, *Humana* v. *Forsyth*, 525 U.S. 299, 313-14 (1999) (citing U.P. *amicus* brief).

SUMMARY OF ARGUMENT

This is a case in which a substantial punitive damage award is not merely within the outer bounds set by the Due Process Clause, but in which the award was *essential* in order to effectuate the duty that petitioner State Farm owed to respondents. The

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[1] Copies of letters from both petitioner and respondents consenting to the submission of any and all *amicus* briefs have been filed with this Court. No counsel for a party authored this brief in whole or in part. No persons or entities other than the *amicus* made a monetary contribution to the preparation or submission of this brief.

law imposes special responsibilities on insurers such as State Farm vis-à-vis their insureds. Insurers are in the business of taking on risk in exchange for money, selling policyholders the promise of financial security. Not atypically, State Farm holds itself out as the "good neighbor" of its policyholders and potential customers.[2]

But the common profit-maximizing incentive that all businesses have creates unique risks in the context of insurance. If the insurer is not sufficiently deterred from doing so, it can invent and implement schemes to minimize its principal expense: payments on claims. An insurer may do so in ways that are difficult to detect, with devastating consequences for the health, livelihood, and homes of insureds. Insurers are accordingly typically held to a duty of "utmost good faith," and punitive damages are uniquely warranted in appropriate cases in order to preserve fealty to the "special relationship between the insurer and insured," which is "inherently unbalanced" against the policyholder. *Egan* v. *Mutual of Omaha Ins. Co.*, 620 P.2d 141, 146 (Cal. 1979).

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[2] Petitioner makes a great deal of "Our Mission, Our Vision, and Our Shared Values":

> State Farm's mission is to help people manage the risks of everyday life, recover from the unexpected and realize their dreams.
>
> *We are people who make it our business to be **like a good neighbor**; who built a premier company by selling and **keeping promises*** through our marketing partnership; who bring diverse talents and experiences to our work of serving the State Farm customer.
>
> *Our success is built on a foundation of shared values -- quality service and relationships, **mutual trust**, **integrity** and financial strength.*
>
> Our vision for the future is to be the customer's first and best choice in the products and services we provide. We will continue to be the leader in the insurance industry and we will become a leader in the financial services arena. *Our customers' needs will determine our path.* ***Our values will guide us.***

State Farm Insurance (visited Oct. 16, 2002) <http://www.statefarm.com/about/mission.htm> (emphases added).

In this case, Petitioner held the fate of its insureds in its hands. Petitioner had the absolute right to control, and did in fact control, the defense of the litigation brought against the Campbells. It also had the specific right to accept or decline a settlement offer within the policy limits. In these special circumstances – where the insurer controls its policyholder's fate entirely, and where the insurer has the power to "gamble" on the risk of a verdict above the policy limits that the policyholder would have to pay out of his own pocket – the courts rightly impose the highest duty of good faith and are willing to impose substantial punitive damages for fraudulent or bad faith conduct by the insurer.

The evidence in this case demonstrates beyond doubt that petitioner utterly capitulated to the temptation to put its own interests ahead of those of its policyholders, in stark contravention of its duty of absolute good faith. State Farm did not merely fail to settle the case at a reasonable time – itself a substantial breach of the insurer's obligations – but instead "engaged in a widespread pattern *of fraud*." Pet. App. 20a (emphasis added). Among other things, the company created an incentive scheme designed to encourage its employees to withhold payments due to insureds on valid claims; it lied to its policyholders; it "routinely destroyed" documents; it targeted its fraudulent activities at its most vulnerable and needy policyholders; and it did so time and again as a matter of company policy. *Id.* 18a-20a. Although the company had previously been hit with a substantial punitive damage award, the amount of that award had not been sufficient to convince the company to change its reprehensible conduct, and more was required to punish and deter these unlawful "ingrained policies of [State Farm's] corporate culture." *Id.* 23a. The record on each of these points is clear.

This case accordingly typifies the rare instances in which a large punitive damage award is essential to provide the financial disincentive that counterbalances the insurer's natural desire to maximize its profits, including particularly through carefully

devised and well-concealed schemes that cut payments of claims owing to policyholders. No amount of bad publicity will ever match the power of a substantial punitive damage award to enforce the insurers' obligation under the law not to put their profits above the interests of their insureds.

ARGUMENT

I. The Unique Duty That Petitioner Owed To Respondents And Its Extraordinary Violation Of That Duty Render Petitioner's Conduct Singularly "Reprehensible."

This Court concluded in *BMW* v. *Gore*, 517 U.S. 559, 575 (1996), that the reprehensibility of a defendant's conduct is "[p]erhaps the most important indicium of the reasonableness of a punitive damages award." Petitioner's conduct in this case was truly reprehensible – indeed, shocking. The Utah Supreme Court explained that this case is unlike any other business tort case because of the "relationship of the parties," and in particular "the degree of confidence and trust placed in the defendant." Pet. App. 24a. The court explained that "[t]he greater the trust placed in the defendant, the more appropriate the imposition of a large punitive damage award for a breach of that trust. A breach of a fiduciary duty also supports a large punitive damage award." *Id.* "Because State Farm breached its duty in this fiduciary relationship, the trial court ruled that State Farm's actions warranted high punitive damages." *Id.* 25a. Indeed, State Farm violated that duty with acts that typify reprehensible conduct: "trickery and deceit" including "deliberate false statements, acts of affirmative misconduct, [and] concealment of evidence of improper motive" (*BMW*, 517 U.S. at 576, 579); and tortious conduct directed at "financially vulnerable" populations (*id.* at 576). "[P]unitive damages are particularly appropriate when fiduciary duty is disregarded and exploited for gain." Pet. App. 25a (citation omitted).

A. Petitioner Owes Insureds Such As Respondents A Duty Of "Utmost Good Faith."

1. The duty of "utmost good faith" that petitioner owed to respondents and breached in this case is far more demanding than the standard commercial duties at issue in this Court's modern punitive damage rulings:

- In four recent cases, the Court has considered punitive damage awards arising from the duties owed between ordinary purchasers and sellers: *BMW* v. *Gore*, 517 U.S. 559 (1996), involved disclosures in the sale of a car; *Honda Motor Co.* v. *Oberg*, 512 U.S. 415 (1994), involved the sale of an unsafe all-terrain vehicle; *TXO Production Corp.* v. *Alliance Resources Corp.*, 509 U.S. 443 (1993), involved the purchase of a leasehold interest in land; and *Pacific Mutual Life Insurance Co.* v. *Haslip*, 499 U.S. 1 (1991), involved the sale of a health insurance policy (as opposed to coverage decisions under the policy).

- The punitive damage awards in two other cases arose from the still more relaxed duties owed by competitors to each other: *Cooper Industries* v. *Leatherman Tool Group*, 532 U.S. 424 (2001), involved a competitor's misuse of the plaintiff's trademark; and *Browning-Ferris Industries* v. *Kelco Disposal*, 492 U.S. 257 (1989), involved a predatory attempt to drive a competitor out of business.

Petitioner, by contrast, owed respondents as insureds a duty of "*utmost* good faith." See Paul Matthews, *Uberrima Fides in Modern Insurance Law*, *in* NEW FOUNDATIONS FOR INSURANCE LAW 39, 39 (F.D. Rose ed., 1987) ("Everyone is aware that insurance is one of the contracts in which there is a 'duty to be of the utmost good faith.'"). As described by the leading treatises, insurers and insureds owe each other this special duty because each is at the mercy of the other, such that a breach warrants "punishment and deterrence." COUCH ON INSURANCE § 198:12 (3d ed. 2001). The insured must not, for example, "provide false or misleading information to the insurer in the application for the policy," while the insurer must "deal with the insured in good faith, *especially* in light of its exclusive duties to defend and settle claims arising under the policy." *Id.* § 198:16 (emphasis added). See also Appleman, INSURANCE LAW AND PRACTICE § 4711 (Berdal ed., 1979).

The duty of utmost good faith has a uniquely distinguished pedigree. The essential role of good faith in law was embraced by the Athenians (as "*epieikeia*") and later by the Romans (as "*aequitas*").[3] Those concepts gave rise not only to the general common law concept of "equity" (J.F. O'Connor, GOOD FAITH IN ENGLISH LAW 2 (1990)), but also to the specific reciprocal obligation owed between insurers and insureds known as *uberrima fides* – *viz.* the duty of "utmost good faith." "The oldest records of insurance contracts have been found in the archives of Genoa and Florence [in the year 1523], where they were * * * identified with risks in sale or loan contracts, particularly as regards carriage by sea." Peter Eggers & Patrick Foss, GOOD FAITH AND INSURANCE CONTRACTS 71 & n.22 (1998). As in England, in "the Italian city-states, * * * the old Roman law concept of good faith between the contracting parties had a great influence on commercial law and practice including marine insurance." Semin Park, THE DUTY OF DISCLOSURE IN INSURANCE CONTRACT LAW 21 (1996).

Mercantile customs – including *uberrima fides* – gave rise to a body of law known as the *lex mercatoria* (the "law of merchants"), which governed the early English insurance contracts in the sixteenth and seventeenth centuries, and took on even greater importance when modern insurance law was born in the eighteenth and nineteenth centuries. Eggers & Foss, *supra*, at 69 & n.5. The rise of the insurance industry centered in London at that time coincided with the appointment of Lord Mansfield as the Chief Justice of the King's Bench and his seminal holding in *Carter* v. *Boehm*, 97 E.R. 1162 (1766), that neither an insured nor an insurer may take advantage of the other by concealing relevant facts. Although the insurer was typically at the mercy of the insured to provide accurate information about the claim, the principle of requiring honesty and fair dealing "would [apply] equally * * * against the under-writer, if he concealed; as, if he insured a ship on her voyage, which he privately knew to be arrived: and an action would lie to recover the premium." *Id.* at 1164. The basis of such an action would be that "[g]ood faith forbids either party by concealing what he privately knows, to draw the other into a bargain." *Id.* The "reason of the rule which obliges parties to disclose, is to prevent fraud, and to encourage good faith." *Id.* at 1165.

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[3] See generally Arnaldo Biscardi, *On Aequitas and Epieikeia*, *in* AEQUITAS AND EQUITY (hereinafter AEQUITAS) 2 (Alfredo Rabello ed., 1997); W.W. Buckland, EQUITY IN ROMAN LAW (1983); Michael Humbert, *The Concept of Equity in the* Corpus Iuris Civilis *and Its Interpretation by Pothier*, *in* AEQUITAS, *supra*, at 29.

Consistent with the English common law, courts in this country have long deemed insurance policies to be "contracts *uberrimae fidei*" (*Stipcich* v. *Metropolitan Life Ins. Co.*, 277 U.S. 311, 316 (1928) (citing *Carter* v. *Boehm*)), requiring "fair dealing by *both* parties" (*Mutual Life Ins. Co.* v. *Hilton-Green*, 241 U.S. 613, 624 (1916) (emphasis added)). See also *M'Lanahan* v. *Universal Ins. Co.*, 26 U.S. 170, 185 (1828) ("The contract of insurance has been said to be a contract *uberrimae fidei*, and the principles which govern it, are those of an enlightened moral policy."); *Massachusetts Mut. Life Ins. Co.* v. *O'Brien*, 5 F.3d 1117, 1121 (CA7 1993) ("[I]nsurance policies are traditionally considered contracts 'uberrimae fidei' – in the most abundant good faith."); *Pereira (In re Payroll Express Corp.)* v. *Aetna Cas. & Sur. Co.*, 186 F.3d 196, 209 (CA2 1999). "The fact that the mutual trust and confidence between the parties are the bases for insurance contracts seems to be the reason for [the] requirement of the duty of *utmost* good faith. It is not possible for the doctrine of *caveat emptor* to be applied to insurance contracts as a result of the * * * fiduciary nature of [those] contracts." Park, *supra*, at 23 (emphasis added). The insurance contract thus imposes "a restraint upon self interest in deference to the interest of others." Daniel Friedmann, *The Transformation of 'Good Faith' in Insurance Law*, *in* GOOD FAITH IN CONTRACT 311, 312 (Roger Brownsword et al. ed., 1999).

And insurers encourage policyholders to place their faith and their futures in the hands of insurance companies. As explained by the Arizona Supreme Court:

> [T]he insurance contract and the relationship it creates contain more than the company's bare promise to pay certain

> claims when forced to do so; implicit in the contract and the relationship is the insurer's obligation to play fairly with its insured. * * * *The industry itself seems to recognize these principles. Advertising programs portraying customers as being "in good hands" or dealing with a "good neighbor" emphasize a special type of relationship between the insured and the insurer – one in which trust, confidence and peace of mind have some part.* * * * We hold, therefore, that one of the benefits that flow from the insurance contract is the insured's expectation that his insurance company will not wrongfully deprive him of the very security for which he bargained or expose him to the catastrophe from which he sought protection.

Rawlings v. *Apodaca*, 726 P.2d 565, 570-71 & n.3 (Ariz. 1986) (emphases added).

2. An insurer's duty of utmost good faith to its insured is particularly important in the context of this case, which presents the insurer's duty to defend and settle litigation that has been filed against its insured, a duty that is at issue in so-called "third-party claims." As the Appleman treatise explains:

> The purpose of insurance is to protect the insured from liability within the limits of the contract by a good faith determination whether the case should be settled; where there is a great risk of recovery beyond the policy limits *the courts cannot allow the insurer to frustrate the purpose of insurance by a cavalier and selfish refusal to settle* and thus expose the insured to judgment beyond the specific monetary protection which his premium has purchased. Thus, *an insurer owes a duty to its insured to exercise the utmost good faith* and reasonable discretion in evaluating the claim, and if the circumstances are such that a reasonable and prudent man with the obligation to pay all of the recoverable damages would settle for the amount within policy limits, it becomes the legal duty of the insurer to do so.

Appleman, *supra*, § 4711, at 395 (emphasis added).

It is thus "easy to see why a liability insurer should be held to stand in a fiduciary position *vis-à-vis* his insured, especially in relation to conduct of the insured's defence." Matthews, *supra*, at 43. See, *e.g.*, *Polselli* v. *Nationwide Mut. Fire Ins. Co.*, 126 F.3d 524, 530-31 (CA3 1997) ("[A]n insurer must act with the utmost good faith toward its insured * * * because the insurance company assumes a fiduciary status by virtue of the policy's provisions which give the insurer the right to handle claims and control settlement."); *Magnum Foods* v. *Continental Cas. Co.*, 36 F.3d 1491, 1504 (CA10 1994) ("[W]hen the insurance company obtains from the insured the power to determine whether an offer of compromise within the policy limits shall be accepted or rejected, this creates a fiduciary relationship between [the two], * * * [who] owe to each other the duty to exercise the utmost good faith.").[4]

This quasi-fiduciary obligation is widely recognized as actionable "as a tort based upon [the insurer's] reservation of control over litigation and settlement which raises a duty to exercise good faith." Appleman, *supra*, § 4712, at 495. "[T]he insured in the third-party setting needs a weapon against the insurer who, having assumed the obligation to protect the insured's interests, might choose to subordinate the insured's interests." Robert H. Jerry, UNDERSTANDING INSURANCE LAW 158 (2d ed. 1996). See also *id.* at 155 ("The primary motivation for recognizing tort duties in third-party insurance was the apparent inadequacy of contract remedies to compensate insureds and deter insurers."). "[T]he cause of action for bad faith in third party cases" has accordingly "received almost unanimous acceptance

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[4] See also, *e.g.*, *Craft* v. *Economy Fire & Cas. Co.*, 572 F.2d 565, 569 (CA7 1978); *Farmers Group, Inc.* v. *Trimble*, 691 P.2d 1138, 1141 (Colo. 1984); *Rova Farms Resort, Inc.* v. *Investors Ins. Co.*, 323 A.2d 495, 505 (N.J. 1974); *Savage* v. *Educators Ins. Co.*, 908 P.2d 862, 865 (Utah 1996).

throughout the United States." Stephen S. Ashley, BAD FAITH LIABILITY (hereinafter Ashley, LIABILITY) § 2.09 (1987).[5]

And this case furthermore presents the single recurring factual scenario that creates the greatest risk that an insurer will breach its quasi-fiduciary duty, and thus the greatest need for courts to punish deviations from the standard of utmost good faith: the insurer's refusal to accept a settlement at or within the policy limits. "Liability insurance contracts have been held to give the insurer absolute authority to settle claims within the policy limits, and the insured has *no power* either to compel the insurer to make such settlements, or to prevent it from doing so." Appleman, *supra*, § 4711, at 368-69 (emphasis added). As described in the "classic" (Stephen S. Ashley, BAD FAITH ACTIONS (hereinafter Ashley, ACTIONS) § 2:05 (1996)) opinion of the Wisconsin Supreme Court in *Hilker* v. *Western Automobile Insurance Co.*, 235 N.W. 413, 414 (1931):

> By the terms of this contract the absolute control of the defense of such actions is turned over to the insurer, and the insured is excluded from any interference in any negotiations for settlement or legal procedure. * * * A duty on the part of the insurer to the insured arises * * * because the insured has bartered to the insurance company all the rights possessed by him to enable him to discover the extent of the injury and to protect himself as best he can from the consequences of the injury.

The insurer's duty of utmost good faith must be enforced rigorously at this point, for the insurer labors under a great conflict of interest: its economic incentive to settle is minimal because its financial exposure is capped by the policy limits, which place the risk of any excess judgment on the insured. There is

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[5] See, e.g., *Continental Ins. Co.* v. *Bayless & Roberts*, 608 P.2d 281, 288 n.10 (Alaska 1980); *Noble* v. *National Am. Life Ins. Co.*, 624 P.2d 866, 868 (Ariz. 1981); *Crisci* v. *Security Ins. Co.*, 426 P.2d 173, 176-77, 179 (Cal. 1967); *Best Place* v. *Penn Am. Ins. Co.*, 920 P.2d 334, 346 (Haw. 1996); *Christian* v. *American Home Assur. Co.*, 577 P.2d 899, 902 (Okla. 1977).

an "inevitable conflict between the insurer's interest to pay as little as possible and the insured's interest not to suffer an excess judgment," for the insurer is in a position to take a "gamble on which only [the] insured might lose." Couch, *supra*, § 203:13. "[B]ecause the insured has relinquished to the insurer the defense of the suit against him, * * * he needs the protection of a tort cause of action to defend himself against the risk that the insurer may wager the insured's financial interests on the possibility of obtaining a defense verdict in the third party's lawsuit." Ashley, ACTIONS § 2:14.

This special circumstance involves a duty of absolute good faith coupled with an extraordinary imbalance in power between insurer and insured over the control of litigation, and an exceptional conflict of interest. That conflict is manifest in the insurer's ability to gamble with the insured's financial well-being by declining a settlement offer at or below the policy limits. Accordingly, an egregious breach justifies an extraordinary punitive damage award in order to punish and to deter bad faith conduct.

Exemplary damages are not merely constitutionally permissible but absolutely *essential* to counterbalance the insurer's incentive to increase its own profits by adopting claims-based practices that put its own interests before that of its insured. As the California Supreme Court explained in the seminal decision of *Egan* v. *Mutual of Omaha Ins. Co.*, 620 P.2d 141, 146 (1979), punitive damages are uniquely warranted to preserve the "special relationship between the insurer and insured," such that in this unique context "[t]raditional arguments challenging the validity of exemplary damages lose force." The court explained:

> As one commentary has noted, "The insurers' obligations are * * * rooted in their status as purveyors of a vital service labeled quasi-public in nature. * * * The obligations of good faith and fair dealing encompass qualities of decency and humanity inherent in the responsibilities of a fiduciary. Insurers hold themselves out as fiduciaries, and with the public's trust must go private responsibility consonant with that trust."

3. Petitioner State Farm unquestionably owed respondents this duty of "utmost good faith." The Campbells were not merely purchasing a car (*BMW*, *supra*) or a piece of property (*TXO*, *supra*), and they manifestly were not in competition with State Farm (*Cooper*, *supra*, and *Browning-Ferris*, *supra*). To the contrary, under Utah law, "when dealing with third parties, the insurer acts as an agent for the insured with respect to the disputed claim. Wholly apart from the contractual obligations undertaken by the parties, the law imposes upon all agents a fiduciary obligation to their principals with respect to matters falling within the scope of their agency." *Beck* v. *Farmers Ins. Exch.*, 701 P.2d 795, 799-800 (Utah 1985).

Here, respondents were "wholly dependent upon [petitioner] to see that, in dealing with claims by third parties, [respondents'] best interests [were] protected." Pet. App. 25a (quoting *Beck*, 701 P.2d at 799)). Petitioner wielded complete control over the litigation against the Campbells, not only by retaining an attorney "who had done a considerable amount of work" (*id.* 4a) for petitioner to defend them, but also by making all decisions regarding the case and the plaintiffs' repeated settlement offers (*id.* 3a-4a). Indeed, petitioner specifically *encouraged* respondents to rely on its control of the litigation: it "affirmatively promised [respondents] that it 'would look out for their best interests' and that they should not procure their own counsel because [petitioner] would take care of them." *Id.* 25a. Petitioner further represented to respondents "that 'they had absolutely no risk,' and even on the chance they were found liable, that they had adequate insurance to cover any potential liability." *Id.*

Notwithstanding its duty to respondents, petitioner refused to settle the case against them despite substantial evidence that Mr. Campbell was at fault (Pet. App. 2a-3a) and repeated offers from the plaintiffs – made both prior to and during trial – to settle for petitioner's policy limits of $25,000 per person or $50,000 per accident (*id.* 3a). The classic conflict between the insurer's lack of incentive to settle the case, because its exposure is capped at the policy limits, and the insured's desire to avoid an excess judgment was squarely presented in this case, as highlighted in a letter to petitioner from counsel for one of the plaintiffs that

urged petitioner to "'tender its limits' because '[a] limit of $25,000 is too low to risk excess exposure by exposing its insured to personal liability.'" *Id.* 3a. As the letter predicted, a judgment substantially in excess of petitioner's policy limits was eventually entered against respondents, and petitioner – through the attorney it had hired to represent respondents – made clear that it did not intend to pay the excess judgment. *Id.* 4a-5a. Only then did respondents "acquire[] other counsel and learn[] that their situation was indeed grave." *Id.*

B. Petitioner's Scheme To Boost Profits By Defrauding Its Insureds Constituted An Extraordinary Violation Of Its Legal Duty Of Utmost Good Faith.

1. Not only did State Farm owe the Campbells a duty of utmost good faith, but the truly reprehensible conduct in which respondent engaged goes far beyond anything seen in this Court's modern punitive damage decisions:

- Two recent cases have arisen from product claims: *BMW* v. *Gore*, 517 U.S. 559 (1996), involved repairs to remedy cosmetic damage to a car; and *Honda Motor Co.* v. *Oberg*, 512 U.S. 415 (1994), involved an ordinary product liability action.

- Two other cases arose from unlawful competitive activity between sophisticated entities that was also covered by regulatory statutes: *Cooper Industries* v. *Leatherman Tool Group*, 532 U.S. 424 (2001), involved trademark infringement against a single plaintiff; and *Browning-Ferris Industries* v. *Kelco Disposal*, 492 U.S. 257 (1989), involved attempts to drive a single competitor out of business.

- In the two cases most analogous to this one – both of which involved far less serious fraudulent conduct – this Court sustained the punitive awards: *TXO Production Corp.* v. *Alliance Resources Corp.*, 509 U.S. 443 (1993), involved a single purchaser's attempt to mislead a single, sophisticated seller; and *Pacific Mutual Life Insurance Co.* v. *Haslip*, 499 U.S. 1 (1991), involved a single employee's misappropriation of client funds.

The breach of duty presented by this case and by petitioner's PP&R policy is far more grave in every salient respect. This case involves not merely State Farm's refusal to settle in a manner that was in the Campbells' best interests but also its conscious attempts to defraud the Campbells, to whom State Farm owed a duty of *utmost* good faith.

When the company's investigator, Ray Summers, reported to his superiors that Mr. Campbell might well have been at fault in causing the collision between Ospital and Slusher, those superiors (Bill Brown and Bob Noxon) covered it up. First, "Brown ordered Summers to change the portion of his report describing the facts of the accident and his analysis of liability." Pet. App. 3a. Then, Noxon "demanded that Summers return to Noxon the letter Noxon had written indicating his approval" of Summers' original report. *Id.* 4a. Finally, the company completed the cover-up by "discontinu[ing] Summers' involvement in the case." *Id.*

State Farm further bolstered its case for refusing to settle by inventing outrageous lies about the accident. One of the company's officials

> instructed the claim adjuster to change the report in State Farm's file by writing that Ospital was "speeding to visit his pregnant girlfriend." There was no evidence at all to support that assertion. Ospital was not speeding, nor did he have a pregnant girlfriend. The only purpose for the change was to distort the assessment of the value of Ospital's claims against State Farm's insured.

Pet. App. 18a.

2. Equally damning, State Farm's breaches of its duty of utmost good faith to the Campbells were firmly established company policy. As the Utah Supreme Court concluded, "State Farm engaged in a widespread pattern of fraud." Pet. App. 20a. The company has long been employing egregious tactics in furtherance of its scheme to avoid paying out claims, including with respect to reasonable settlement offers: "For over two decades, State Farm has set monthly payment caps and individually

rewarded those insurance adjusters who paid less than the market value for claims. Agents changed the contents of files, lied to customers, and committed other dishonest and fraudulent acts in order to meet financial goals." *Id.* 18a.

These tactics are an entrenched part of the company's approach to dealing with liability lawsuits by "harass[ing] and intimidat[ing] opposing claimants, witnesses, and attorneys." Pet. App. 19a. The company uses its size and wealth to carry out these policies. *Id.* ("State Farm actually instructs its attorneys and claim superintendents to employ 'mad dog defense tactics' – using the company's large resources to 'wear out' opposing attorneys by prolonging litigation, making meritless objections, claiming false privileges, destroying documents, and abusing the law and motion process."). In all, "State Farm repeatedly and deliberately deceived and cheated its customers via the PP&R scheme." *Id.* 18a.

Importantly, the company singles out other persons like the Campbells, who are among its most vulnerable policyholders. "As the trial court found, State Farm's fraudulent practices were consistently directed to persons–poor racial or ethnic minorities, women, and elderly individuals–who State Farm believed would be less likely to object or take legal action." Pet. App. 18a-19a.

The Utah Supreme Court concluded that punitive damages are essential because State Farm engages in further deception to shield other policyholders from ferreting out its unlawful acts. Thus, "State Farm's own witnesses testified that documents were routinely destroyed so as to avoid their potential disclosure through discovery requests. Such destruction even occurred while this litigation was pending." Pet. App. 19a. Another State Farm tactic is to avoid recordkeeping practices that could help outsiders uncover the PP&R scheme. *Id.* ("State Farm, as a matter of policy, keeps no corporate records related to lawsuits against it, thus shielding itself from having to disclose information related to the number and scope of bad faith actions in which it has been involved.") In these ways, "State Farm engaged in deliberate concealment and destruction of all documents related to this profit scheme." *Id.*

3. The Utah Supreme Court also recognized that no previous efforts have been able to stop State Farm's practices. Even a large award of punitive damages has had no effect. See Pet. App. 17a ("State Farm's corporate headquarters had never learned of, much less acted upon, a punitive damage award of $100 million in a previous case."). State Farm's failure to change its ways reflects how entrenched its tactics have become:

> In light of State Farm's decades-long policy of fraudulent and dishonest practices in its handling of claims, it is difficult to imagine how such ingrained policies of corporate culture can be easily or quickly changed. This would be true even in a case where the perpetrator was fully aware of and remorseful for its conduct. State Farm has not exhibited any such self-awareness in this case. Instead, State Farm asserted at trial that its PP&R policy was "obsoleted" in 1992 and again in 1994. However, the Campbells' evidence showed that the policy was still being followed at the time of trial.

Id. 23a.

These circumstances plainly present the very strongest possible case for a substantial punitive damage award – one larger than the verdicts that had previously failed to get State Farm's attention – in order to punish and to deter its outrageous conduct. Petitioner adopted a policy virtually calculated to defy its "obligations of good faith and fair dealing" and the "qualities of decency and humanity inherent in the responsibilities of a fiduciary." *Egan* v. *Mutual of Omaha Ins. Co.*, 620 P.2d 141, 146 (Cal. 1979). Its conduct clearly warrants "punishment and deterrence." COUCH ON INSURANCE § 198:12.

4. The unique and extraordinary nature of State Farm's fraud is apparent not only from the facts as found below but also by comparing this case with others in which courts have addressed insurers' bad faith refusal to settle third-party claims. A comprehensive review of both state and federal case law since 1990 reveals many examples of bad faith – conduct of the sort that the Utah Supreme Court's decision will have the beneficial effect of

deterring – but those examples involve insurers' conduct towards individual policyholders. In those cases, courts have tended to limit damage awards.

As these examples reflect, *amicus* has been unable to uncover any other instance in which an insurer has implemented such a widespread, pernicious scheme to avoid paying out meritorious claims and to defraud its own policyholders. Thus, to the extent that the award in this case is truly extraordinary, it is entirely justified because State Farm's conduct is entirely without parallel:

- In *The Birth Center* v. *The St. Paul Cos.*, 787 A.2d 376 (Pa. 2001), the insurer ignored both the recommendations of three different judges that it settle a medical malpractice action against its insured for the policy limits of one million dollars and warnings from defense counsel that the verdict could be substantial. Instead, the insurer refused to settle, explaining that it "tries 'all of these bad baby cases, and we're going to trial.'" *Id.* at 392. Although the insurer later paid both its policy limits and the excess verdict, the Pennsylvania Supreme Court affirmed a bad-faith award of $700,000 against the insurer.

- In *California Union Insurance Co.* v. *Liberty Mutual Insurance Co.*, 920 F. Supp. 908 (N.D. Ill. 1996), the district court found that Liberty Mutual (as the primary insurer) had acted in bad faith in refusing to settle a personal-injury suit against its insured. *Id.* at 912. Following a jury verdict in the insured's favor, Liberty Mutual paid its policy limits of two million dollars, while California Union – the excess insurer – paid $3.7 million. The district court emphasized that, although Liberty Mutual had "admittedly received strong signals from all sources * * * that the probability of an adverse finding on liability [was] great and the amount of damages would exceed the policy limits," the insurer never made any serious effort prior to trial to determine whether the plaintiff would settle for an amount that was more than its $800,000 offer but still within the policy limits. *Id.* (internal quotations omitted).

- In *Lozier* v. *Auto Owners Insurance Co.*, 951 F.2d 251 (CA9 1991), the Ninth Circuit upheld a $3.5 million award

against the insurer for its bad-faith refusal to settle a lawsuit arising from a car accident that left the appellant a quadriplegic. The court of appeals noted that the appellant was "likely to get 'a substantial verdict in excess of policy limits,'" while the insurer had "never investigated the accident * * * until its own money was at stake" (*id.* at 254), had not undertaken the relevant legal research (*id.* at 254-55), and – in contrast to the insured's "potential financial risk of more than $900,000" – faced a maximum liability of $100,000. *Id.* at 255. Most significantly, however, the court of appeals found that the insurer "put its own interests first at every stage": "[w]hen [the insured] was facing catastrophic liability, [the insurer] was slow and stingy. But when Auto Owners itself was facing the same liability, it was timely and generous." *Id.* at 255.

• In *Great American Insurance Co.* v. *International Insurance Co.*, 753 F. Supp. 357 (M.D. Ga. 1990), International – an excess insurer – alleged that the primary insurer, Great American, had rebuffed a pre-trial offer to settle a lawsuit brought against the insured for its policy limits of $250,000.[6] After the jury returned an award of $4.1 million (subsequently reduced to $400,000 by the trial court), the case eventually settled for one million dollars, half of which was paid by International. In ruling that Great American had acted in bad faith, the district court emphasized that the insurer had refused to settle even when confronted with "overwhelming evidence indicating that its original assessments of the case were incorrect and that there existed a strong possibility that a verdict substantially beyond its policy limits would be rendered against its insured." *Id.* at 362-64.[7]

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[6] As *Great American* and other cases demonstrate, encouraging primary insurers to act in good faith to settle valid claims against their insureds will *benefit* the insurance industry because an insurer's bad-faith refusal to settle in some instances harms an excess insurer liable for any award exceeding the primary policy limits.

[7] See also, *e.g.*, *New England Ins. Co.* v. *Healthcare Underwriters Mut. Ins. Co.*, 295 F.3d 232, 235 (CA2 2002) (bad-faith refusal to settle when primary insurer was "aware early on of weaknesses in the case" and knew that refusal to settle would expose both excess insurer and insured, but nonetheless failed to make any settlement offer); *Highlands Ins. Co.* v. *Continental Cas. Co.*, 64 F.3d 514 (CA9 1995) (bad-faith refusal to settle for less than policy limits in light of insurer's conclusion that insured was at fault, as well as repeated warnings that verdict would likely exceed limits); *Maryland Cas. Co.* v. *Dixie Ins. Co.*, 622 So. 2d 698 (La. App. 1 Cir. 1993) (bad-faith refusal to settle lawsuit when insured's liability obvious, insured exposed to larger verdict as result of punitive damages claim against him, and insurer had failed to inform insured of either offer to settle or punitive damages exclusion in policy).

II. The Fact That Petitioners' Conduct Was Part And Parcel Of A Fraudulent Nationwide Policy Whereby Valid Claims Were Arbitrarily And Deceptively Rejected In First- And Third-Party Cases Alike Makes This Case All The More Deserving Of A Substantial Punitive Damage Award.

The Utah Supreme Court rightly considered the full scope of State Farm's fraudulent scheme that led to the breach of faith in the specific case before it – a scheme to underpay claims and reject reasonable settlements, including through an incentive system designed to put the company's financial interests above its duties to its policyholders, all implemented through an extraordinary pattern of outright fraud. To the end of exposing and evaluating the nature and extent of that fraudulent scheme, the Utah courts properly admitted evidence of State Farm's wrongful conduct in other jurisdictions in dealing not only with third-party, but also first-party, claims by its insureds. The reprehensible nature of petitioner's acts is apparent and fully parallel with respect to each: State Farm's failure to comply with its duties to its insureds, its cover-ups, its lies, and its document destruction are unethical and unlawful *whatever* the context.

State Farm's policy of defrauding its insureds in first- and third-party cases through the same set of incentives was itself egregious, but was rendered all the more reprehensible when, as in the case at bar, it was applied with utter indifference to the special quasi-fiduciary duty that State Farm owed to insureds in third-party cases. For example, in imposing punitive damages

on a bus company for an accident caused by excessive speed that injured children in its care, a court surely may consider the fact that the company had an outrageous, categorical rule of driving fifty miles per hour whatever the circumstances. The facts that sometimes the bus company operated on highways with even higher speed limits, sometimes carried adult passengers, and sometimes traveled into other states that recognize no special duty under the circumstances do not detract from the conclusion that the company's policy broadly and consciously breached the special duty it owed in the circumstances. Similarly, in imposing punitive damages on a hospital for fraud by overcharging nursing home patients for whom it holds a power-of-attorney, a court surely could consider the fact that the hospital had a policy of overcharging *all* its patients by ten percent, notwithstanding that most patients had not conferred a power of attorney and that some of the patients actually owed the hospital more money than it had overcharged them.

Although the Utah Supreme Court thus properly sustained the jury's punitive damage award in this case in order to punish and deter unlawful conduct in that one state, petitioner is simply wrong to contend that the Due Process Clause renders Utah powerless to enter an award designed to prevent State Farm from launching such conduct from its corporate headquarters at all – even though the effect of State Farm's *ceasing* to do so would necessarily be to spare victims in states other than Utah. Any extraterritorial consequences of the ruling below are either irrelevant or sufficiently tied to tortious activity within Utah to fall easily within the bounds of the Due Process Clause. There is a substantial risk that, absent a severe penalty, a national company with State Farm's track record of grossly unethical acts towards its insureds would continue its illegal conduct in Utah by arbitraging penalties for bad faith refusal to settle third-party claims in that one state through profits from other jurisdictions and from the bad faith refusal to settle first-party claims. The prospect of arbitrage is most logically (and at the least constitutionally) measured by reference to the defendant's own policy – here, its PP&R policy, which applies throughout the country and to first-party as well as third-party claims.

The states have never been restricted to imposing punitive damages measured only by the harm to the individual plaintiff before the court. It is a basic principle that exemplary damages are appropriate precisely when a case does

> not present an isolated wrong on the part of some person, attributable perhaps to passing anger or passion and unlikely to occur again, but instead it discloses the perpetuation of a fraud purposely and deliberately done and sought to be justified on the ground of conformity by defendant with what is said to be a common trade practice followed by dealers in used automobiles at the expense of the general buying public.

Jones v. *West Side Buick Co.*, 93 S.W.2d 1083, 1089 (Mo. App. 1936) (per curiam).

States accordingly have long considered the full range of a defendant's misconduct in determining the proper amount of punitive damages.[8] In *Grimshaw* v. *Ford Motor Co.*, 174 Cal. Rptr. 348 (Cal. Ct. App. 1981), for example, a multi-million-dollar punitive damage award was based on the fleet-wide cost savings reaped by Ford from failing to remedy the vulnerability of the Pinto fuel tank. *See id.* at 391 (considering "the savings [Ford] realized in deferring design modifications in the Pinto's fuel system"). The court saw the nationwide misconduct of the defendant as an aggravating factor, not as a reason to limit punitive damages: "Unlike malicious conduct directed toward a single specific individual, Ford's tortious conduct endangered the lives of thousands of Pinto purchasers" throughout the country. *Id.* at 388.

Similarly, in *Hawkins* v. *Allstate Ins. Co.*, 733 P.2d 1073 (Ariz.), *cert. denied*, 484 U.S. 874 (1987), a multi-million-dollar punitive damage award against an auto insurer was upheld when the plaintiff presented evidence that the insurer had engaged in deceptive claims practices throughout the country for years, by shaving small amounts from each insured's total loss claim filed.

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[8] See, *e.g.*, Clarence Morris, *Punitive Damages in Tort Cases*, 44 HARV. L. REV. 1173, 1187 (1931).

733 P.2d at 1085. In particular, the insurer routinely deducted a thirty-five-dollar cleaning fee, even though cars that had been completely demolished were not in fact cleaned. *Id.* at 1078. The insurer instructed its claims representatives to make such deductions under the theory that "if you could save one dollar on a million claims, you'd save the company as much as a million dollars." *Id.*[9]

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[9] See also *Eichenseer* v. *Reserve Life Ins. Co.*, 934 F.2d 1377, 1383 (CA5 1991) (concluding that punitive award of $500,000 was warranted because earlier $150,000 award had "had little deterrent effect"); *O'Gilvie* v. *International Playtex, Inc.*, 821 F.2d 1438, 1446 (CA10 1987) (upholding $10 million punitive damage award in toxic shock death on basis of nationwide conduct and profits), *cert. denied*, 486 U.S. 1032 (1988); *General Motors Corp.* v. *Moseley*, 447 S.E.2d 302, 312 (Ga. App. 1994) (rejecting Commerce Clause challenge to jury's consideration of defendant's out-of-state conduct); *Hospital Auth. of Gwinnett County* v. *Jones*, 409 S.E.2d 501, 503 (Ga. 1991), *cert. denied*, 502 U.S. 1096 (1992) (considering possible harm to other victims of defendant's policy in upholding $1.3 million punitive damage award); *Gryc* v. *Dayton-Hudson Corp.*, 297 N.W.2d 727, 741 (Minn. 1980) (justifying $1 million punitive damage award in part on ground that the defendant "reaped substantial profits through the sale of its highly flammable cotton flannette," without determining whether product was considered defective in states where sales occurred), *cert. denied*, 449 U.S. 921 (1980); *Star Credit Corp.* v. *Ingram*, 347 N.Y.S.2d 651, 652, 654 (N.Y. Civ. Ct. 1973) (awarding full amount of punitive damages requested when evidence showed that defendant finance company had implemented consumer fraud scheme victimizing thousands of low-income residents over many years); *Wangen* v. *Ford Motor Co.*, 294 N.W.2d 437, 462 (Wis. 1980) (punitive damages assessed on basis of Ford's failure to remedy defective gas tanks on numerous 1967 Mustangs). See also *Moore* v. *American United Life Ins. Co.*, 197 Cal. Rptr. 878, 887, 895 (Cal. Ct. App. 1984) (upholding $2.5 million punitive damage award—83 times compensatory award of $30,000—when evidence established that defendant insurer engaged in a pattern and practice of cheating insured out of health benefits: "where compensatory damages, based on policy limits, are modest, but where the jury heard evidence of fraudulent claims practices potentially affecting numerous insureds other than the plaintiffs, strong reliance on the reasonable relation rule may defeat the object and purpose

This case is moreover critically different from *BMW* v. *Gore*, 517 U.S. 559 (1996), on the question of extraterritoriality because State Farm had no reason to believe that its fraudulent conduct was lawful outside of Utah. The core elements of the PP&R policy were impermissible in *every* jurisdiction. Bad faith refusal to settle third-party claims and State Farm's other gravely unethical conduct – including document destruction and misleading its insureds – give rise to tort liability in every state. Bad faith refusal to settle even first-party claims is actionable for more than ordinary breach of contract in more than three-quarters of the states[10] and in contract in the remainder, but the relevant point is that in *every* state it is regarded as a violation of a legal duty.

III. State Tort Liability And Punitive Damages Have A Particularly Critical Role To Play In Punishing And Deterring Wrongdoing In The Insurance Context.

1. When Congress passed the McCarran-Ferguson Act, it left to the states the responsibility of regulating insurance. The Act provides that "[n]o Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance," because

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of punitive damages"); *Delos* v. *Farmers Group, Inc.*, 155 Cal. Rptr. 843, 857 (Cal. Ct. App. 1979) (upholding punitive damage award based in part on "an inextricable involvement with conduct aptly described * * * as a nefarious scheme to mislead and defraud thousands of policyholders" (internal quotations omitted)).

[10] Stephen S. Ashley, BAD FAITH ACTIONS § 2:15 (1996) ("Recent decisions * * * have tipped the scales decisively in favor of the first-party tort and have clearly established it as the majority rule."); *id.* (Supp. 1997) § 2:15. Thirty-one states provide that bad faith gives rise to a cause of action in tort (AK, CT, NV, NC, ND, OH, OK, SC, TX, AZ, AL, CO, DE, ID, DC, IA, KY, NE, NM, RI, SD, WY, MT, WA, AR, CA, IN, HA, VT, MS, NY); two require the action to be brought "on the contract" but expressly permit broad categories of damages that are rarely available in ordinary contracts cases (UT, WV); and seven others have statutes giving rise to special causes of action based on bad faith (GA, LA, PA, NH, FL, MA, IL).

"the continued regulation and taxation by the several States of the business of insurance is in the public interest." 59 Stat. 33, as amended, 61 Stat. 448. The Act "le[ft] regulation to the States [because] the States were in close proximity to the people affected by the insurance business and, therefore, were in a better position to regulate that business than the Federal Government." *Federal Trade Comm'n* v. *Travelers Health Ass'n*, 362 U.S. 293, 302 (1960); *see also id.* at 303 (Harlan, J., dissenting) (noting that in "the McCarran-Ferguson Act, * * * Congress pervasively restored to the States the regulation of the business of insurance").

Although states bear the responsibility, it does not follow that they are able to fulfill it effectively, for insurance regulators have remarkably few enforcement powers, and they face numerous other political and financial obstacles to holding insurers to their duty of absolute good faith. Indeed, "many state insurance departments are hopelessly underfunded and understaffed and are sometimes unable to carry out basic regulatory functions adequately, much less oversight of complex international insurance networks." Susan Randall, *Insurance Regulation in the United States: Regulatory Federalism and the National Association of Insurance Commissioners*, 26 FLA. ST. U. L. REV. 625, 699 (1999). Insurers effectively have free rein from regulation because "in dealing with unfair insurance practices, administrative agencies have often demonstrated inertia, and legislative bodies, by and large, have displayed a seeming indifference." William M. Shernoff et al., INSURANCE BAD FAITH LITIGATION § 8.01 (1984).

A leading exposé, which features a chart labeled "Why State Regulation is a Joke," furthermore demonstrates that state insurance regulation suffers from industry capture. It concludes that "insurers and agents * * * dominate the regulatory system that is supposed to police them," due to the "revolving door between the insurance industry and insurance commissioners." *How the Insurance Industry Collects an Extra $65 Billion a Year from You by . . . Stacking the Deck*, MONEY MAGAZINE, Aug. 1996, at 50. A typical chief insurance commissioner of a state comes to that job from a major insurance company – a company to which

the person fully expects to return upon completing the regulatory stint. *Id.* One such chief retained ownership of his insurance company during his time as commissioner, enabling him to "enrich his own company" by, *e.g.*, "approving rate increases." Another chief devoted his term not to protecting consumers but instead to "unshackl[ing] insurers from nettlesome rules." *Id.* A third – who was excoriated by consumer groups for being not merely "a shill for the industry" but the embodiment of "the industry" itself – stated openly that he does not believe in regulating insurers: "'The spartan forces of the marketplace will protect consumers.'" *Id.*[11]

There is thus a broad recognition that state agencies which regulate insurance "are inefficient, lethargic, poorly funded, under-staffed, and highly exposed to varying political whims." Willy E. Rice, *Race, Gender, "Redlining," and the Discriminatory Access to Loans, Credit, and Insurance*, 33 SAN DIEGO L. REV. 583, 698 (1996). See also Robert E. Keeton & Alan I. Widiss, INSURANCE LAW § 8.1(b) at 935 (1988) ("[S]tate insurance departments have continually been hampered by inadequate funding * * * and inefficient personnel."); Suzanne Woolley & Gail DeGeorge, *Policies of Deception? Investigations of Misleading Sales Tactics Rock the Insurance Industry*, BUS. WK., Jan. 17, 1994, at 24-25 ("States can rarely muster the resources needed for extensive investigations."); Katie Cook Morgan, Comment, *Leaving the Management of "Managed Care" up to the States*, 65 U. CIN. L. REV. 225, 248-49 (1996) ("The notion that regulation of the insurance industry can best be handled solely by the states is no longer workable. * * * The insurance industry has outgrown the state insurance departments and has,

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[11] The article also highlights that petitioner State Farm created a "fake grass-roots" effort on its own behalf by spending millions of dollars on a group that is misleadingly named People for a Fair Legal System. The group, which receives "70% of its funding from State Farm and works out of a building that houses State Farm offices," pushes "tort reform measures that would limit the damages juries can award in lawsuits."

in the process, become unaccountable as to many of the negotiations in which it engages.").

2. State tort law, and the availability of punitive damages in particular, obviously take on greater significance in the context of such a predictable if episodic regulatory vacuum. It is precisely because "relief for unjust and unfair insurance practices has not been forthcoming from sources outside the judiciary" that the "significance of the deterrent effect of punitive damages is perhaps heightened." Shernoff, *supra*, § 8.01. "There has long been evidence of understaffing and inadequate resources in state insurance departments, despite ostensibly thorough regulation. * * * Moreover, state insurance regulators may be susceptible to lobbying by insurance and other political interests that may not be consonant with the interests of policyholders. Private attorneys general, and plaintiffs generally, are not subject to such influences." Theodore Allegaert, Comment, *Derivative Actions by Policyholders on Behalf of Mutual Insurance Companies*, 63 U. CHI. L. REV. 1063, 1086 (1996). See also *White* v. *Unigard Mut. Ins. Co.*, 730 P.2d 1014, 1019 n.3 (Idaho 1986) ("[T]he statutory scheme to regulate the insurance industry fails to provide sufficient incentive," due in part to the fact that "[t]he Department of Insurance has limited means with which to police the insurance industry. * * * [S]tatutes regulating the insurance industry do little to encourage the settlement of large claims *unless they are backed up with an action for bad faith*.") (emphasis added).

Punitive damages, in particular, encourage injured persons to serve as private attorneys general and thus to vindicate society's interest in curbing harmful conduct. See *Neal* v. *Newburger Co.*, 123 So. 861, 863 (Miss. 1929) (punitive damages "awarded to the injured party as a reward for his public service in bringing the wrongdoer to account"); David G. Owen, *Punitive Damages in Products Liability Litigation*, 74 MICH. L. REV. 1257, 1289 n.158 (1976) ("Many economists have recognized the advantages of private, 'victim' enforcement of the law. They suggest that it is a most, and in some cases the only, effective means of enforcing the law of private transactions 'precisely because the incentives to the enforcers are as large as the incentives to pro-

spective violators.'" (quoting Gary S. Becker & George J. Stigler, *Law Enforcement, Malfeasance, and Compensation of Enforcers*, 3 J. LEGAL STUD. 1, 6 (1974))); Bruce Chapman & Michael Trebilcock, *Punitive Damages: Divergence in Search of a Rationale*, 40 ALA. L. REV. 741, 788 (1989) ("one can easily see possible advantages of private enforcement" of the law through the imposition of punitive damages, *e.g.*, that "private enforcers are likely to be more efficient[,] * * * more motivated and more cost conscious" than "state bureaucrats"); Dan B. Dobbs, *Ending Punishment in "Punitive" Damages: Deterrence-Measured Remedies*, 40 ALA. L. REV. 831, 887 (1989); Marc Galanter & David Luban, *Poetic Justice: Punitive Damages and Legal Pluralism*, 42 AM. U. L. REV. 1393, 1441-42 (1993); Jack M. Sabatino, *Privatization and Punitives: Should Government Contractors Share the Sovereign's Immunities From Exemplary Damages?*, 58 OHIO ST. L.J. 175, 212-13 (1997).

States are furthermore entitled to rely on punitive damages as an important supplement to the criminal law. Such damages are essential to punish and deter wrongdoing that is clearly tortious, even if the wrongdoer is careful to tailor its wrongdoing so as to take advantage of the inevitable gaps in the extant body of criminal law and the protective shield of the *ex post facto* clause. On State Farm's contrary view, states would be left to the following choices: (1) leaving harms to their citizens unremedied and undeterred; or (2) trying to bridge the shortfall in enforcement by passing new laws and new regulations, and drastically expanding the state bureaucracy needed to prosecute offenders who would otherwise be free to prey on the public. Especially in a time of limited state budgets, the second option would be a difficult one for many jurisdictions.

3. Finally, there is no merit to the contention that state law punitive damage awards actually redound to the *detriment* of policyholders. That argument lacks support in either logic or the empirical evidence. Shernoff, *supra*, § 8.09. First, "[m]any states have statutory and administrative provisions that regulate insurance rates and specify the factors that may be considered in determining premiums for various types of policies." *Id.* Such provisions would rule out increasing premiums based upon ad-

verse judgments and awards of punitive damages for bad faith. Second, "even assuming that the insurer is not legally precluded from raising premiums, it can be argued that only the individual insurer that is subjected to a large punitive damages award is likely to raise premiums," and that its competitors will not. *Id.* Indeed, as the California Supreme Court has explained in rejecting the claim "that substantial awards of punitive damages against insurers are to be discouraged because such awards will be 'passed on' to consumers in the form of higher future premiums,"

> the principles upon which the American system of free enterprise is based would suggest to the contrary – *i.e.*, that other companies would proceed to capitalize upon the resulting competitive advantage. If the ultimate result is to cause the offending company to lose business to those whose practices have not been such as to subject them to substantial punitive awards, it would seem that the object of deterrence will be well served – resulting in an ultimate benefit to insurance consumers as a whole.

Neal v. Farmers Ins. Exch., 21 Cal. 3d 910, 929 n.14 (1978).

CONCLUSION

Amici respectfully suggest that the judgment of the Utah Supreme Court should be affirmed.

Respectfully submitted,

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